



ASSOCIATION OF AMERICAN RAILROADS

Law Department

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Senior Vice President-Law
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November 28, 2011

Honorable Cynthia T. Brown
Chief, Section of Administration
Surface Transportation Board
395 E St., S.W.
Washington, DC 20423

231-104

Re: STB Finance Docket No. 35506, Western Coal Traffic League—Petition for
Declaratory Order

Dear Ms. Brown:

Pursuant to the Board's order served September 28, 2011, attached please find the Reply
Comments of the Association of American Railroads (AAR) for filing in the above proceeding.

Respectfully submitted,

Louis P. Warchot
*Counsel for the Association of
American Railroads*

ENTERED
Office of Proceedings

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Public Record

Attachment

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Finance Docket No. 35506

WESTERN COAL TRAFFIC LEAGUE—PETITION FOR DECLARATORY ORDER

REPLY COMMENTS OF THE
ASSOCIATION OF AMERICAN RAILROADS

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Introduction

In a decision served September 28, 2011, the Surface Transportation Board (“Board”) initiated a declaratory order proceeding to address the effect of the price that Berkshire Hathaway, Inc. (“Berkshire”) paid to acquire BNSF Railway Company (“BNSF”) in 2010 on both the Board’s annual BNSF Uniform Railroad Costing System (“URCS”) and annual BNSF revenue adequacy determinations. The proceeding was initiated in response to a petition filed May 2, 2011 by the Western Coal Traffic League (“WCTL”) requesting that the Board deviate from Generally Accepted Accounting Principles (“GAAP”) in establishing BNSF’s post-acquisition net investment base and instead declare that “it will exclude the write-up in BNSF’s net investment base attributable to the difference between the book value and the price that [Berkshire] paid to acquire BNSF in 2010, and make corresponding changes in BNSF’s annual URCS depreciation calculations.” *Id.* In its Order, the Board invited public comment on the

issues raised and requested that parties address the effect of the subject net investment base write-up on the annual revenue adequacy determinations and annual URCS for BNSF beginning in the year 2010.¹

The AAR filed opening comments on October 28, 2011 urging the Board to deny WCTL's petition for declaratory order. The AAR noted that the use of acquisition costs to value BNSF's post-acquisition net investment base conforms with GAAP and is required under 49 U.S.C. §§ 11142 and 11161 and the Board's implementing regulations.² The AAR further noted that use of acquisition costs is also supported by longstanding Board and Interstate Commerce Commission ("ICC") precedent,³ the findings of the Railroad Accounting Principles Board ("RAPB")⁴, and has been endorsed by the courts.⁵ The AAR also noted that there is no evidence to doubt that the purchase price paid by Berkshire for the acquisition of BNSF was negotiated at arms-length by commercially sophisticated business entities and "represents by far the best evidence of the market value" of the BNSF's net asset base at the time of acquisition.⁶ The AAR accordingly urged the Board to follow long-standing statutory and regulatory requirements, as well as clear agency and judicial precedent, supporting use of GAAP to value BNSF's net

¹ Whether or not the calculations at issue affect the annual revenue adequacy calculation for BNSF, the calculations do not resolve the broader and more complex determination of whether a rail carrier is long-term revenue adequate. See e.g., *Railroad Revenue Adequacy—1984 Determination*, 1 I.C.C.2d 615, 620 (1986).

² 49 U.S.C. § 11142 requires that the Board, in prescribing its Uniform System of Accounts ("USOA") for use by rail carriers, "[t]o the maximum extent practicable, ... conform such system to generally accepted accounting principles." 49 U.S.C. § 11161 similarly requires that the Board conform its cost accounting rules to GAAP "to the maximum extent practicable." The Board's implementing regulations conform to these statutory requirements by prescribing use of acquisition costs for rail purchase transactions. See 49 C.F.R. § 1201.2-15.

³ See, e.g., *CSX Corp.—Control—Conrail, Inc.*, 3 S.T.B. 196, 262-65 (1998) ("*Conrail*"); *Railroad Revenue Adequacy—1988 Determination*, 6 I.C.C. 2d 933, 935-42 (1990) ("*Railroad Revenue Adequacy*").

⁴ See *Railroad Accounting Principles, Final Report*, Volume II -Detailed Report at 45-48 (RAPB) (Sept. 1, 1987).

⁵ See, e.g. *Assoc. of Amer. RR's v. ICC*, 978 F. 2d 737, 741-43 (D.C. Cir. 1992); *Erie-Niagara Rail Steering Comm. v. STB*, 247 F. 3d 437, 442-43 (2d Cir. 2001) ("*Erie-Niagara*").

⁶ See *Conrail*, 3 S.T.B. at 265.

investment base for purposes of URCS costing and annual revenue adequacy determinations in this proceeding. See AAR Opening Comments at 3-4.

Opening comments were also filed in this proceeding by BNSF, WCTL, the National Industrial Transportation League ("NITL"), various other shipper organizations, and the U.S. Departments of Agriculture ("USDOA") and Transportation ("USDOT"). For the reasons stated in the AAR's opening comments, the AAR strongly endorses BNSF's arguments supporting the use of GAAP to value its post-acquisition net investment base for purposes of URCS costing and annual revenue adequacy determinations. The parties asking the Board to deviate from statutory and regulatory requirements and clear precedent supporting use of GAAP have presented no basis for the Board doing so. The AAR accordingly urges the Board to reject the arguments challenging the use of GAAP in this proceeding.

Discussion

The Board has a clear administrative duty to apply applicable statutory and regulatory requirements (including its prescribed cost accounting rules used for regulatory purposes) in a uniform manner to all affected carriers.⁷ Those statutory and regulatory requirements are equally applicable to BNSF in this proceeding, and there is no sound basis presented here for the Board to decline to follow them.

As noted *supra*, the use of GAAP in purchase transactions to value the post-acquisition net investment base of the acquired carrier is required by ICCTA and the Board's own rule. The Board's rule conforms to the recommendations of the RAPB, was adopted by notice and comment rulemaking, and was in fact supported by NITL and other electric utility participants in

⁷ The applicable statutory provisions pertaining to the Board's cost-accounting rules used for regulatory purposes specifically require that the Board may adopt reasonable rules "prescribing expense and revenue accounting and reporting requirements consistent with [GAAP] *uniformly applied to such carriers*." 49 U.S.C. § 11164.

the rulemaking as representing the most accurate measure of the purchased carrier's post-acquisition net investment base for costing and other regulatory purposes.⁸

For over two decades, the Board (and the ICC) have consistently followed the applicable statutory and regulatory requirements by using GAAP to measure the post-acquisition net investment base of the acquired carrier (and the true economic cost of providing services). The agency's rule requiring use of GAAP was uniformly applied regardless whether a party (carrier or shipper) claimed that use of acquisition cost would undervalue or overvalue the post-acquisition net investment base in the regulatory proceeding.⁹ In each of these cases, the Board stressed that, in the absence of *actual evidence* demonstrating that the acquisition cost was not "an accurate reflection of the worth of that property,"¹⁰ acquisition cost "represents by far the best evidence of the market value" of the acquired carrier's net investment base at time of acquisition.¹¹ The agency's uniform application of GAAP in such proceedings was consistently upheld on judicial review as conforming to statutory and regulatory requirements and as rationally based.¹²

⁸ See *Railroad Revenue Adequacy*, 6 I.C.C. 2d at 938-39. The AAR and various other carriers opposed the Board's rule based on their view that acquisition cost would consistently undervalue a rail carrier's net investment base due to the then-depressed state of the railroad industry. The ICC rejected the carriers' argument but allowed a carrier to demonstrate on a case-by-case basis that the acquired carrier's net investment base at time of acquisition was in fact artificially depressed by applicable agency regulatory policies. *Id.* at 937-38, 941.

⁹ See, e.g., *Railroad Revenue Adequacy*, 6 I.C.C. 2d at 941; *Conrail*, 3 S.T.B. at 265; *Rio Grande Industries, Inc.—Control—Southern Pac. Transp. Co.*, 4 I.C.C. 2d 834, 980 (1988) ("*Rio Grande*").

¹⁰ See *Railroad Revenue Adequacy—1988 Determination*, 6 I.C.C.2d at 942 ("[T]here is nothing to indicate either that BN's acquisition of the Frisco was anything other than the result of arm's length negotiations or that the price BN paid was held down by the specter of governmental action. Thus, in the case of BN, we cannot conclude that predecessor cost provides a more accurate measure of value than does acquisition cost."); see also *Conrail*, 3 S.T.B. at 265 ("Protestants have submitted no evidence to support the notion that the purchase price that was negotiated at arm's length for Conrail is not an accurate reflection of the worth of that property.").

¹¹ See *Conrail*, 3 S.T.B. at 265; see also *Railroad Revenue Adequacy*, 6 I.C.C. 2d at 940-41 (1990).

¹² See cases cited note 2, *supra*.

The AAR submits that agency rules serve an important regulatory purpose and that the Board has a clear administrative duty to follow its own rules¹³ (as well as ICCTA statutory directives) in this proceeding. The purpose of agency rules is to provide uniformity and consistency in the agency decision-making process as well as to provide clear guidance and predictability to the railroad industry and other parties participating in Board proceedings. The Board's rule requiring the use of acquisition costs to value the post-acquisition net investment base of the acquired carrier provides such uniformity, consistency and predictability in conformity with its purpose.

Moreover, the use of acquisition cost to value BNSF's post-acquisition net investment base in this proceeding "comports with GAAP" and there is no evidence that it "has been inflated and does not accurately reflect the fair market value of the assets."¹⁴ The arguments of WCTL and other parties in this proceeding provide no valid or economically sound basis for the Board to deviate from GAAP as providing the most accurate measure of BNSF's post-acquisition net investment base here.¹⁵ In such circumstances, the Board has a clear administrative responsibility to uniformly and even-handedly apply its rule requiring use of GAAP to value BNSF's post-acquisition net investment base in this proceeding, and the AAR urges that the Board do so.

¹³ See *Service v. Dulles*, 354 U.S. 363, 372 (1957) (agency has duty to follow its own regulations); *Thomas Brooks Chartered v. Burnett*, 920 F.2d 634, 642 (10th Cir. 1990) (*accord*).

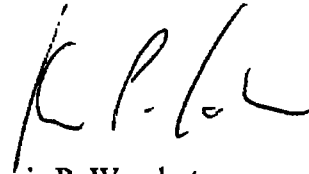
¹⁴ See note 6, *supra*. In this proceeding, neither WCTL nor the other shipper organizations contest that the Berkshire acquisition of BNSF was an arm's length transaction by sophisticated parties nor that use of GAAP provides the most current and accurate measure of BNSF's post-acquisition net investment base.

¹⁵ See STB Ex Parte No. 582 (Sub-No. 1), *Major Railroad Consolidation Procedures*, Slip op. at 28; 2001 WL 648944, * 18 (served June 11, 2011) (Board noted that "there is no sound economic justification" for valuing properties obtained through a merger based upon predecessor book values rather than acquisition cost.")

Conclusion

WCTL's petition for declaratory order should be denied.

Respectfully submitted,



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